IN THE

Supreme Court of the United States

OCTOBER TERM, 1977

No. 77-753

INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA,
Petitioner,

v.

JOHN DANIEL,
Respondent.

No. 77-754

LOCAL 705, INTERNATIONAL BROTHERHOOD OF TEAMSTERS, CHAUFFEURS, WAREHOUSEMEN AND HELPERS OF AMERICA, AND LOUIS PEICK,
Petitioners,

v.

JOHN DANIEL,
Respondent.

On Writs of Certiorari to the United States Court of Appeals for the Seventh Circuit

MOTION OF ERISA INDUSTRY COMMITTEE (ERIC) FOR LEAVE TO FILE A BRIEF *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS AND BRIEF *AMICUS CURIAE* OF THE ERISA INDUSTRY COMMITTEE (ERIC) IN SUPPORT OF THE PETITIONERS

PETER G. NASH
GEORGE J. PANTOS
1750 Pennsylvania Ave., N.W.
Washington, D.C. 20006

THOMAS L. O'BRIEN
ARTHUR B. SMITH, JR.
115 South LaSalle Street
Chicago, Illinois 60603

Counsel for ERISA Industry Committee, amicus curiae

Of Counsel:

VEDDER, PRICE, KAUFMAN, KAMMHOLZ & DAY
1750 Pennsylvania Ave., N.W.
Washington, D.C. 20006
(202) 393-5970

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases Page

TABLE OF AUTHORITIES—Continued

Page

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

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MOTION OF ERISA INDUSTRY COMMITTEE (ERIC) FOR LEAVE TO FILE A BRIEF *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

To the Honorable Chief Justice and Associate Justices of the Supreme Court of the United States:

The ERISA Industry Committee (ERIC) respectfully moves this Court, pursuant to Supreme Court Rule 42(3), for leave to file the accompanying brief in this case as *amicus curiae* in support of the Petitioners and urging reversal of the decision of the Court of Appeals for the Seventh Circuit. In support of this motion, ERIC shows as follows:

1. This motion is necessitated by the refusal of the Respondent to consent to the filing of a brief by ERIC as *amicus curiae.*

2. The ERISA Industry Committee (ERIC) is a non-profit corporation, composed of 83 United States corporations and representing a cross-section of the nation's largest firms in such industries as automobile manufacturing, electrical manufacturing, retailing, steel, photographic equipment, metals, insurance, banking, telephone, pharmaceuticals, chemicals, petroleum, airlines, rubber, utilities, and various service industries. These corporations for years have maintained one or more retirement plans for the benefit of their employees, many of which plans have been negotiated with unions. In all, these 83 corporations sponsor over 750 retirement plans covering approximately 8.5 million participants (employees, retirees and other beneficiaries) which is more than 20 percent of all employees covered by private retirement plans.[1] Retirement plans sponsored by ERIC members

[1] Comprehensive data regarding private pension and welfare programs and persons covered by them is not available. The statistics cited herein regarding plans of ERIC members have been principally derived from the Plan Descriptions

pay benefits to some 1.5 million retirees and other beneficiaries. Plans with over 1,000 participants represent slightly over ten percent of defined benefit retirement plans, but cover over eighty percent of all participants in such plans; and plans with over 10,000 participants represent less than one percent of defined benefit retirement plans, but cover over one-half of all participants in such plans.[2] Most ERIC members sponsor plans with more than 10,000 participants and ERIC generally represents a cross-section of the employee benefit plan sponsors which provide the significant majority of all plan benefits.

(Forms EBS-1) filed with the Labor Department. It is generally accepted that there are somewhere between 30 and 45 million participants in private pension programs. *See, e.g.,* H.R. Rep. No. 807, 93d Cong., 2d Sess. 3 (1974); S. Rep. No. 383, 93d Cong., 1st Sess. 2-3 (1973); Statement of Gregory J. Ahart, Director, Human Resources Division, United States General Accounting Office, before the Subcomm. on Retirement Income and Employment of the House Select Comm. on Aging at 2 (Feb. 27, 1978). Participants in pension plans sponsored by ERIC members are not less than 15% of all participants in private pension programs and might be as many as 25% of such participants. ERIC members sponsor nearly one-quarter of the five hundred largest retirement plans, ranked by assets. Derived from listing of the 500 largest plans, Pensions & Investments, Jan. 2, 1978 at 5. The 500 largest plans had assets as of December 31, 1976, of approximately $120 billion, according to this listing. *Id.* at 1.

[2] 2 PBGC Ann. Rep. 18 (1975-76). Defined benefit plans, which are the only plans subject to PBGC jurisdiction, account for about 20% of the estimated 470,000 pension plans, but cover about 75% of the estimated 30 million pension plan participants. Statement of Gregory J. Ahart, *supra* note 1, at 2.

Through ERIC, these companies coordinate their views and provide information and recommendations to government on how the private pension system functions, and on the impact of government regulations and interpretations under the Employee Retirement Income Security Act of 1974 ("ERISA") on retirement plan participants and plan sponsors. This includes rendering assistance to courts in their deliberations on significant employee retirement plan issues of broad concern to employers. Indeed, ERIC filed a brief as *amicus curiae* with the Seventh Circuit in the case now before this Court and this Court granted ERIC's motion and accepted ERIC's brief as *amicus curiae* in support of the petition for certiorari in this case (Order of February 21, 1978).

3. ERIC does not contend that the Plaintiff should not be granted his pension benefits on other grounds not before this Court. In that sense we take no position on the ultimate dispute between Plaintiff and Defendants. Rather, ERIC requests permission of this Court for leave to file as *amicus curiae* in order to address the novel legal proposition now before the Court stressing its impact upon employers such as those represented by ERIC.

4. As decided by the court of appeals,[3] this case stands for the proposition that an employee's participation in a retirement plan, which covers him automatically at no cost to him, is subject to the antifraud provisions of the Securities Acts of 1933 and 1934. As a consequence, the failure to provide

[3] *Daniel* v. *International Brotherhood of Teamsters*, 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 46 U.S.L.W. 3512 (Feb. 21, 1978).

an employee with certain information, never before thought to be material, has and wil render unions, employers, plans and plan administrators liable for massive money damages. Although the Seventh Circuit's decision involves only a claim against the Plaintiff's union and its retirement fund, that decision does raise the prospect of similar liability for employers.

5. Because no employer, union, trustee, plan administrator or, indeed, the Congress or Securities and Exchange Commission ever has understood that the antifraud provisions apply generally to such retirement plans, the Seventh Circuit's decision raises the prospect of such persons becoming subject to claims for billions of dollars and may encourage extensive vexatious litigation under the securities acts. Further, the decision may severely disrupt collective bargaining in a manner contrary to our nation's labor policy and will create significant administrative problems for retirement plan administrators.

6. No employer is involved as a party in this case. Accordingly, the interests of employers concerned with the administration of retirement plans may well be unrepresented in this Court's consideration of the case unless our request to file the accompanying brief is granted.

WHEREFORE, it is respectfully moved and requested that the ERISA Industry Committee (ERIC) be granted leave to file the accompanying brief as *amicus curiae*.

Respectfully submitted,

PETER G. NASH
GEORGE J. PANTOS
1750 Pennsylvania Ave., N.W.
Washington, D.C. 20006

THOMAS L. O'BRIEN
ARTHUR B. SMITH, JR.
115 South LaSalle Street
Chicago, Illinois 60603

Counsel for ERISA Industry Committee, amicus curiae

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BRIEF *AMICUS CURIAE* OF THE ERISA INDUSTRY COMMITTEE (ERIC) IN SUPPORT OF THE PETITIONERS

The ERISA Industry Committee (ERIC) hereby submits this brief in Case Nos. 77-753 and 77-754 urging reversal of the decision of the United States Court of Appeals for the Seventh Circuit entered in this case on August 20, 1977.

INTEREST OF *AMICUS CURIAE*

A statement describing ERIC and its interest in this case is set forth in the preceding motion requesting leave to file this brief *amicus curiae*.

SUMMARY OF ARGUMENT

This case involves the question of whether an employee's participation in an involuntary, noncontributory retirement plan is, under the Securities Acts of 1933 and 1934, a security which is sold to the employees in the normal course of their employment.

It might be possible by wooden logic and literal interpretation to cast an employee's interest in a retirement plan as a "security" covered by the securities acts, but that result would conflict squarely with this Court's decision in *United Housing Foundation, Inc.* v. *Forman*, 421 U.S. 837 (1975) where economic reality rather than superficial linguistic analysis was employed as the keystone for defining a "security" covered by the securities acts. In addition, it is clear that Congress never intended that an employee's interest in a retirement plan be a "security" covered by the securities acts.

In 1958, Congress enacted a statute which required employers to disclose information to employees covered by retirement plans. Thus, Congress initially proceeded in its regulations of pensions in much the same way as it had earlier regulated securities transactions under the securities acts by requiring disclosure while declining to set substantive minimum standards. That effort failed, because many employees were prevented from obtaining anticipated benefits by overly strict plan requirements, not lack of disclosure.

Congress then changed direction, and in 1974, following nearly ten years of study, enacted ERISA, which set certain substantive minimum standards for private retirement plans while requiring that specific information be provided to employees and the government at specified times. However, in considering these new standards and disclosure requirements, Congress was sensitive to the fact that this nation's private retirement system is a voluntary one and that no employer is required by law to provide retirement benefits to its employees. To insure that employers would continue to have the incentive to start, maintain and expand retirement plans, Congress carefully tailored ERISA's requirements so that they would neither be too costly nor overburden employers with administrative red tape.

The decision of the Seventh Circuit will require the payment of damages or retirement benefits even to an employee, who has not met reasonable eligibility requirements which conform to ERISA's minimum standards, if his plan fails to make currently unknown disclosures required by the securities acts. The Seventh Circuit has thus clearly disregarded ERISA's goal of strengthening the private pension system by preserving employer incentives to start and continue retirement plans. Since almost no plans have made the disclosures held to be material by the Seventh Circuit, affirmance of its judgment could

impose liability of between \$23.8 billion and \$39.6 billion on retirement plans, employers, and unions threatening their financial destruction as well as the job and retirement expectations of millions of present workers.

With potential claims of billions of dollars, extensive and costly litigation will result, further decreasing the incentives to maintain and expand the private pension system. Adding to this concern is the lack of any case or statutory guidance to what must be disclosed regarding any involuntary, noncontributory pension plan.

The lower court's ruling, if affirmed, would also negate ERISA's broad preemption of state law by permitting the states to regulate interests in retirement plans as "securities," placing unwarranted and unnecessary administrative burdens on plan sponsors.

Further, the Seventh Circuit's conclusion that the securities acts apply to retirement plans as if employment decisions were investment decisions affronts common sense, ignores the economic reality of the employment relationship, and disregards the basic distinction between capital and labor in our industrial society.

Even if the securities acts themselves, prior judicial opinions and the subsequent ERISA legislation would permit affirmance of the decision of the circuit court, the serious adverse consequences of such a decision on collective bargaining and basic labor policy militate against such a course.

The Seventh Circuit's opinion creates such a threat of litigation and liability that any prudent employer who bargains retirement benefits with a union will feel compelled to attend any meeting of employees set to ratify the collective bargaining agreement in order to insure that the employees are given full and accurate information and are made aware of how much higher their current wages might be but for the proposed retirement plan coverage. Such action, however, will substantially undercut the union's role as the exclusive bargaining agent for all employees, a role which is essential to effective labor-management relations in our country and a role which this Court has defended against lesser attacks in the past.

Finally, if a union which bargains retirement benefits is to be held liable for damages and is to be subjected to lawsuits such as the one now before this Court, it is not unreasonable to assume that unions will simply decline to bargain about retirement plans. Such a step would clearly be adverse to employee interests and is inconsistent with our national labor policy.

ARGUMENT

I. Introduction

The Plaintiff in this case, John Daniel, worked 22½ years as a member of Local 705 of the Teamsters Union and was covered during that period by a union-negotiated Teamster retirement plan which required 20 years of unbroken service by a covered employee before he became entitled to retirement benefits. When Daniel retired he did not qualify for benefits because he had been laid off for a short

period of time some 16 years prior to his retirement. Daniel then commenced the present suit to obtain retirement benefits from his union for himself and for a class of employees who have participated in Teamster pension funds.

Although Daniel's complaint alleges various causes of action which, if proven, may support the relief he desires, only the two counts involving the antifraud provisions of the securities acts are before this Court. These two counts allege that the defendants have violated the antifraud provisions of the Securities Acts of 1933 [1] and 1934 [2] and consequently are required to pay the Plaintiff his full retirement benefits. In support of this claim, Daniel contends that his union misled the employees it represented by failing to disclose to them the various circumstances which would have precluded them from receiving retirement benefits, the actuarial grounds upon which the funds were based, and the actuarial likelihood that a participant would not receive any pension benefits at all.

Defendants moved to dismiss these two counts but the trial court denied the motion, and the court below affirmed. *Daniel* v. *International Brotherhood of Teamsters*, 410 F.Supp. 541 (N.D. Ill. 1976), *aff'd*, 561 F.2d 1223 (7th Cir. 1977), *cert. granted*, 46 U.S.L.W. 3512 (Feb. 21, 1978). In so doing, the Seventh Circuit ruled that an employee's interest in

[1] 15 U.S.C. § 77(a), *et seq.* (1970).

[2] 15 U.S.C. § 78(a), *et seq.* (1970).

a noncontributory,[3] involuntary [4] retirement plan is a "security" for purposes of the antifraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934. The court below also held that an employee accepts an "offer of sale" of a "security" (an interest in a retirement plan) and, accordingly, acquires a right to full disclosure of all material information concerning that plan when (1) the employee commences employment with an employer who offers a retirement plan; (2) the employee votes with his fellow workers to accept a collective bargaining agreement negotiated by his union representative which provides for a retirement plan; or (3) the employee continues to work for his employer. 561 F.2d at 1242, 1243, 1249. The Seventh Circuit determined that the "material" information to be disclosed on each of those occasions must include, at least the actuarial probability that a participant actually will receive pension benefits and factors such as risk of loss, breaks in service, death before retirement age and plan termination that can cause a member to be deprived of benefits. 561 F.2d at 1228-29, 1248. If all material information is not provided to an employee, the court below ruled that the employee may maintain a cause of action for money damages, which Plaintiff asserts may include the full payment of otherwise unearned retirement benefits.

It is not difficult to understand and appreciate the Seventh Circuit's reaction to Daniel's failure to re-

[3] The Teamster plan is "noncontributory" in that all contributions are made by employers, and employees are neither required nor permitted to contribute to the plan.

[4] The Teamster plan is "involuntary" in that participation in the plan is a condition of employment.

ceive retirement benefits. Six salient aspects of this case, however, place it in proper perspective.

First, Daniel's complaint seeks relief on grounds other than those now before this Court, so that it is by no means necessary for him to prevail here in order to obtain the relief he seeks.

Second, Daniel did not contribute his money to the retirement plan, nor did he choose to be covered by the plan. Instead, contributions to the plan were made by his employer and the plan automatically covered him simply because he worked there.

Third, this case does not involve only Daniel, but instead is a class action seeking retirement benefits for a large number of Teamster-represented employees. In addition, as we show below, Daniel's suit affects all of this nation's private retirement plans.

Fourth, although the case before this Court involves alleged violations of the antifraud provisions of the securities acts, Daniel's basic claim does not involve "fraud" in the popular sense, but, instead, alleges a failure to provide certain information presumably required by the securities acts, but at a time when no one, including the Securities and Exchange Commission, believed that the securities acts required disclosures to retirement plan participants. 561 F.2d at 1226-27. *See Robinson* v. *UMW Health and Retirement Funds*, 435 F.Supp. 245, 247 (D.D.C. 1977).

Fifth, this case is not a suit to require disclosure of information to retirement plan participants; it is a suit for money damages in the form of retirement benefits. The courts below have not granted requests for information; they have set the stage for money

damage claims that may bankrupt retirement plans, unions and employers nationwide.

Sixth, national policy as expressed in the Employee Retirement Income Security Act of 1974 ("ERISA") prevents a loss of benefits, such as Daniel experienced, from occurring in the future.

In fulfilling its task of deciding "which of the myriad financial transactions in our society come within the coverage" of the securities acts this Court should give due consideration to these observations. *United Housing Foundation, Inc.* v. *Forman*, 421 U.S. 837, 848 (1975). Furthermore, the Seventh Circuit's failure to properly accommodate settled principles of labor law and established interpretations of the securities acts, as well as the direct conflict between that court's decision and congressional policy embodied in ERISA, must inform the Court's judgment and compel a reversal of the lower court.

II. Application Of The Securities Acts To Involuntary Non-contributory Pension Plans Is Inconsistent With Policies Underlying ERISA And Has Substantial And Destructive Implications.

We believe that all Congress has said and done from its early deliberations regarding retirement benefit plan regulation through the enactment of ERISA clearly establishes that Congress proceeded with a clear understanding that the securities acts neither did nor should control, apply to, or affect involuntary, noncontributory retirement plans.[5]

[5] We do not suggest, as the Seventh Circuit thought, that ERISA "repeals" the application of the securities acts to re-

Indeed, the consideration of ERISA, regarded as the most sweeping retirement plan legislation ever adopted, involved the study, investigation, hearings and debate of four committees of Congress, as well as three Cabinet departments, and input from countless employee organizations, corporations and individuals. Yet, during this entire legislative and executive effort dealing with all aspects of employee participation in retirement plans, there is no hint that Congress ever intended or believed that the securities laws were generally applicable to such plans and merely were being supplemented by this complex and detailed new law.[6]

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tirement plans. 561 F.2d at 1246. Rather, we contend that this Court properly may look to what Congress said and did in enacting ERISA in 1974 as an indication that Congress never intended the earlier securities acts to cover retirement plans in the first place. *See Pipefitters* v. *United States*, 407 U.S. 385, 411-13 (1972); *NLRB* v. *Allis-Chalmers Mfg. Co.*, 388 U.S. 175 (1967). Indeed, when it suited the Seventh Circuit's purposes to recognize that subsequent legislative action can be a guide to determining earlier legislative intent, the court did so in this case. 561 F.2d at 1237 n. 26 and accompanying text.

[6] The Interim Report of Activities of Private Welfare and Pension Plan Study ("Interim Report") marked the beginning of the deliberations of ERISA by Congress and was adopted as a "complete description of the federal regulation affecting the administration of private [pension] plans . . . ." S. Rep. No. 127, 93d Cong., 1st Sess. 4 (1973). The Interim Report states that:

> Pension and profit-sharing plans are exempt from coverage under the Securities Act of 1933 . . . , unless the plan is a voluntary contributory pension plan and invests in the securities of the employer company an amount greater than that paid into the plan by the employer. A voluntary contributory plan is one to which both the employee and the employer contribute and in which employees voluntarily participate. If the plan's investment in the employer's securities exceeds the employer's contribution, both the employer's securities and the interest in the plan must be registered under the Securities Act with the SEC.

S. Rep. No. 634, 92d Cong., 2d Sess. 96 (1971). *See also*, ERISA Leg. Hist., Vol. I at 587, 589; Vol. II at 2348, 2350, 3377, 3470; Vol. III at 4748. All citations to ERISA legislative history shall be the separately bound legislative history: Senate Comm. on Labor and Public Welfare, Subcomm. on Labor, 94th Cong., 2d Sess., Legislative History of the Employee Retirement Income Security Act of 1974 (Three Volumes) (1976) [herein cited as "ERISA Leg. Hist."].

Indeed, this same understanding existed when Congress considered the bills which led to the adoption of the Welfare and Pension Plans Disclosure Act of 1958, 29 U.S.C. §§ 301-309 (1970) (repealed by Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1031(a)(1) (Supp. V 1975) ("WPPDA"). *See* S. Rep. No. 1734, 84th Cong., 2d Sess. 60 (1956); S. Rep. No. 1440, 85th Cong., 2d Sess. 9, *reprinted in* [1958] U.S. Code Cong. & Ad. News 4137, 4145. One such bill, S. 1122, would have vested enforcement responsibility in the SEC, but the SEC professed lack of expertise. Hearings on S. 1122 Before the Subcomm. on Welfare and Pension Plans Legislation of the Senate Comm. on Labor and Public Welfare, 85th Cong., 1st Sess. 119 (1957).

Statements of the legislative sponsors of ERISA since the circuit and district court decisions in this case have affirmed anew their understanding that the securities acts never were intended to cover retirement plan interests generally. Statement of Congressman Dent, 174 Daily Labor Rep. (BNA) at A-6 (Sept. 7, 1976); Letter from Senator Williams to SEC Chairman Williams (Dec. 13, 1977), 168 Pens. Rep. (BNA) at R-19—R-22 (Dec. 19, 1977); Statements of Senator Williams and Senator Javits in sponsoring S. 3017, 85 Daily Labor Rep., Special Supp. (BNA) at 2-3, 8 (May 2, 1978).

Further, contrary to the assertion of the Seventh Circuit, the antifraud provisions of the securities acts cannot be read as complementary to the requirements of ERISA.[7] 561 F.2d at 1248. The argument that the securities laws fill a gap left by ERISA in that they require disclosure prior to an "investment decision," *e.g.*, a decision to accept employment or vote to ratify a collective bargaining agreement, while ERISA permits disclosure to be made up to 90 days after an employee becomes a plan participant[8] (561 F.2d at 1248-49) simply will not withstand analysis. That argument is based upon a misreading of the history of retirement plan regulation in this country and is directly counter to the objectives of the Congress as reflected in legislation regulating retirement plans.

National policy and the public interest favor the institution and continuation of private retirement plans. The decades following the conclusion of the

[7] *See generally* the excellent analysis in Comment, *Application of the Federal Securities Laws to Noncontributory, Defined Benefit Pension Plans,* 45 U. of Chi. L. Rev. 124 (1977).

[8] In recent testimony before the Senate Human Resources Committee, Subcommittee on Labor, SEC Chairman Williams conceded that disclosure in the form of a summary plan description as required by ERISA within 90 days after employment was as adequate as pre-employment disclosure. Oversight of ERISA, 1977: Hearings on S. 2125 Before the Subcomm. on Labor of the Comm. on Human Resources, 95th Cong., 1st Sess. 113-114 (1977) (Statement of Chairman Harold M. Williams). In addition, if disclosure under the securities laws were desirable, the registration requirements, which are the core of securities law disclosures, also should apply. However, as noted by the Seventh Circuit, the SEC maintains that 96% of all pension plans are exempt from registration. 561 F.2d at 1250 n. 61.

Second World War witnessed a constantly accelerating growth of private retirement plans, both in the number of plans and the extent of coverage. Employers willingly established and made contributions to such plans. Employees, solely by reason of their employment and continued service, became participants in such plans. These employees developed certain hopes and expectations of future retirement income and designed their life styles accordingly. Thus, the basic hope for substantial retirement income became an expectation of the American worker which Congress deemed worthy of protection.

On the other hand, our American retirement plan system, other than Social Security and similar statutory programs, was born, flourished and continues as a voluntary system in which employers are free to provide or not to provide for the retirement of their employees. In order for such a voluntary system to continue, there must be incentives for employers to provide retirement benefits. One such incentive is the employer's desire to retain employees, thus requiring some length of employee service before an employee receives his benefit or is free to move on and retain his vested retirement benefit. Another incentive is that an employer may establish a retirement plan which will provide benefits for longer service employees at a relatively low cost and with a minimum of administrative red tape. Throughout its deliberations leading to the enactment of the Welfare and Pension Plans Disclosure Act of 1958, 29 U.S.C. §§ 301-309 (1970) (repealed by Employee Retirement Income Security Act of 1974, 29 U.S.C. § 1031(a)(1) (Supp. V 1975) and, ultimately, ERISA, Congress was acutely aware of the need to

strike a balance between these competing considerations. The entire structure of the safeguards established by Congress for retirement plans indicates a clear appreciation that, although certain standards specifically designed to protect retirement plan participants were necessary, it was just as necessary to retain incentives to encourage employers to institute and continue such plans.

Congress' first major effort at regulating the private retirement plan system was the WPPDA which required that certain information be disclosed to retirement plan participants—a relatively slight burden on employers. Congress, thus, chose the same kind of regulation that it had earlier applied to the sale of securities when it enacted the Securities Acts of 1933 and 1934.

But Congress' first effort did not work. Indeed, in enacting ERISA, Congress made the express legislative judgment that a system of disclosure such as that embodied in the WPPDA or the securities laws was an inadequate and inappropriate remedy to the problems of the private pension system. As the Senate Report accompanying S. 4 found:

> After a comprehensive investigation of abuses in the administration and investment of private fund assets, Congress adopted the Welfare and Pension Plan Disclosure Act of 1958. The policy underlying enactment of this Act was purportedly to protect the interests of welfare and pension plan participants and beneficiaries through disclosure of information with respect to such plans. . . .
>
> Experience in the decade since the passage of the above amendments has demonstrated the inadequacy of the Welfare and Pension Plans Disclosure Act in regulating the private pension system for the purpose of protecting rights and benefits due to workers. It is weak in its limited disclosure requirements and wholly lacking in substantive fiduciary standards. . . .

ERISA Leg. Hist., Vol. I at 590.

Thus, disclosure had not prevented plan participants like Daniel [9] from losing accrued pension benefits because of a short break-in-service. As the Senate Report further noted:

> The fact that statutory rules exist says little as to their efficacy in adjusting inequities that

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[9] The entire legislative history is replete with examples closely paralleling the facts now before this Court. *See, e.g.*, ERISA Leg. Hist., Vol. III at 3584, 4656, 4749-51, 4790. The avowed central purpose of ERISA was, and is, to bring relief to employees whose expectations (as opposed to technical rights under existing retirement plans) had proven to be only false hopes. *See, e.g.*, 29 U.S.C. § 1001(a) (Supp. V 1975); ERISA Leg. Hist., Vol. I at 90-92, 1267; Vol. II at 1599, 3474; Vol. III at 4282-83, 4657. Significantly, on two separate occasions in which the need for retirement benefit protection to be afforded by ERISA was being debated in Congress, Senator Bentsen urged its adoption as a step necessary to protect American working men and women from the following:

> Another example of unreasonable vesting requirements involves the participants of a union-administered pension plan in Chicago. Each local within this union administers its own pension plan. Under the terms of these plans, a worker must remain within the same local for 20 years in order to acquire any vested rights. Sometimes a slight shift in jobs—perhaps from a loading dock to the weighing station—involves a shift in union locals and a complete loss of all pension rights for an employee with less than 20 years on the first job.

ERISA Leg. Hist., Vol. II at 1634, Vol. III at 4792.

> are visited upon plan participants, as evidenced by the hearings before this Committee. In almost every instance, participants lose their benefits not because of some violation of federal law [the disclosure requirements of the WPPDA], but rather because of the manner in which the plan is executed with respect to its contractual requirements of vesting or funding. . . . Thus, under present law, accumulated pension credits can be lost even when separated employes are within a few months, or even days, of qualifying for retirement.

Id. at 591.

To remedy these problems,[10] ERISA provided *substantive* standards regulating participation, vesting, the computation of service, breaks-in-service and accrual of benefits.[11] The legislative decision to protect the interests of pension participants through substantive standards meant disclosure could be restricted to specific items necessary for the enforcement of those substantive standards.

But in deciding what substantive standards and specific disclosures would be required by ERISA,

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[10] What Congress perceived as the other major problem of the pension system—inadequate funding—also was dealt with through substantive regulation. ERISA established minimum funding standards which include controls on the actuarial methods to be used, 29 U.S.C. §§ 1081-86 (Supp. V 1975); 26 U.S.C. § 412 (Supp. V 1975), and created the Pension Benefit Guaranty Corporation which guarantees the payment of minimum benefits to a participant if the plan is terminated before vested benefits are fully funded. 29 U.S.C. § 1301, *et seq.* (Supp. V 1975).

[11] 29 U.S.C. §§ 1052-54 (Supp. V 1975); 26 U.S.C. §§ 410-12 (Supp. V 1975).

Congress had to strike a balance between protecting employee retirement expectations and maintaining incentives for employers to start, continue and expand retirement plans and benefits. Without the latter, fewer and fewer workers would be covered by private retirement plans. The key incentives were (1) maintaining reasonable costs for employers who sponsor and pay for private retirement plans for their employees, and (2) holding administrative red tape, record keeping and documentation to a minimum so as not to overburden plan sponsors and administrators.

These congressional concerns were underlined by Representative Ullman, now Chairman of the House Ways and Means Committee:

> I want to emphasize that these new [ERISA] requirements have been carefully designed to provide adequate protection for employees and, at the same time, provide a favorable setting for the growth and development of private pension plans. It is axiomatic to anyone who has worked for any time in this area that pension plans cannot be expected to develop if costs are made overly burdensome, particularly for employers who generally foot most of the bill. This would be self-defeating and would be unfavorable rather than helpful to the employees for whose benefit this legislation [ERISA] is designed.

ERISA Leg. His., Vol. III at 4673.

The House Committee on Education and Labor in reporting ERISA legislation stated:

> The Employee Benefit Security Act as reported by the Committee is designed to remedy certain

defects in the private retirement system which limit the effectiveness of the system in providing retirement income security. The primary purpose of the bill is the protection of individual pension rights, but the Committee has been constrained to recognize the voluntary nature of private retirement plans. The relative improvements required by this Act have been weighed against the additional burdens to be placed on the system. While modest cost increases are to be anticipated when the Act becomes effective, the adverse impact of these increases have been minimized. Additionally, all of the provisions in the Act have been analysed on the basis of their projected costs in relation to the anticipated benefit to the employee participant.

ERISA Leg. Hist., Vol. II at 2348. *See also*, ERISA Leg. Hist., Vol. II at 1601, 1645, 1648, 1649, 2352-56, 3493; ERISA Leg. Hist., Vol. III at 4797.

In the Senate floor debate on the Conference Report, Senator Nelson clearly delineated the careful balance struck by Congress in enacting ERISA:

> In all its deliberations and decisions, Congress was acutely aware that under our voluntary pension system the cost of financing pension plans is an important factor in determining whether a pension plan will be adopted. Unduly large increases in cost can impede the progress of the private pension system. For this reason, in the case of those requirements which add to the cost of financing pension plans, Congress tried to adopt provisions which strike a balance between providing a meaningful protection for the employees and keeping costs within reasonable limits for employers.

ERISA Leg. Hist., Vol. III at 4800.

Indeed, in early debate upon the proposed legislation, Senator Williams responded to Senator Hartke's efforts to impose more stringent and costly requirements upon pension and benefit plans by facetiously asking Senator Hartke if he was proposing an amendment requiring all employers to provide pension benefits. Senator Williams went on to note:

> Mr. President, until the Senator does impose upon employers the mandate to have pension plans, I would think that all of the provisions that the Senator would offer, put together, would just kill off any attitude on the part of the employers who do not have any pensions to come on in.

ERISA Leg. Hist., Vol. II at 1776.

Further, since the passage of ERISA, Congress has been attentive to the increased costs and administrative burdens created by that legislation and various members have expressed their concern about the adverse impact of ERISA upon the start of new plans and the continuation of existing plans. For example, the House Small Business Committee recently published the results of a questionnaire sent to small businesses which intended to terminate existing retirement plans. Some 79 percent of those businesses indicated that ERISA had an effect upon their decision. Of those businesses 92 percent were motivated, at least in part, to terminate plans because of the increased costs mandated by ERISA. House Small Business Comm. ERISA Questionnaire Results, 160 Pens. Rep. (BNA) at A-2—A-3, R-11—R-13 (Oct. 24, 1977).

Senators Williams and Javits recently have introduced legislation, S. 3017, to correct some of the ad-

verse effects of ERISA on retirement plan starts and terminations. In doing so, Senator Williams stated:

> It is my view that private retirement plans are and must continue to be a critical component in America's system of providing retirement income. Yet, even after 25 years of spectacular growth of these plans in the years following the Second World War, private pension plans in 1974 covered only about half of the private sector, non-agricultural work force. Since ERISA's enactment in 1974, growth of the private system has slowed, and the past 3½ years have been a time of an increased incidence of terminations, and a decreased incidence of new plan starts, accompanied, however, by steady growth of the size of the work force.

85 Daily Labor Rep., Special Supp. (BNA) at 3 (May 2, 1978).

In sum, a critical objective of ERISA was and is to permit retirement plans to be operated at low cost with a minimum of administrative burdens,[12] so that

[12] In support of S. 3017, Senator Javits has said:

> By making ERISA easier to live with, these amendments should encourage employers to maintain their existing plans and to establish new plans. I believe, however, that further encouragements and incentives are necessary in order to expand the numbers of workers covered by private pension plans.
>
> . . . .
>
> My bill's most far-reaching change in ERISA's reporting and disclosure sections is to grant the new Commission authority to exempt any employee benefit plan from any of the existing paperwork requirements or to modify any of these requirements.
>
> . . . .

there is a continuing incentive for employers to start, and expand retirement plans and benefits. The consequences of the Seventh Circuit's judgment, however, emasculates this clear and sound objective of Congress, for that judgment has created substantial disincentives to retirement plan development.

The theory on which the judgment of the Seventh Circuit rests, though focused on Daniel's plight, logi-

[12]

> This new authority will give the Commission needed flexibility in tailoring reporting and disclosure requirements to particular situations. The Commission will be able to exercise its discretion to reduce unnecessary paperwork which adds to the cost of plan administration and may not be essential to protecting the interests of participants and beneficiaries.
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> . . . .
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> My bill also eliminates a number of requirements which appear not to be cost-justified. The summary annual report, which must be distributed to participants each year and which must disclose, among other things the plan's assets and liabilities as well as its annual receipts and disbursements, is eliminated because it is too costly in light of the information it provides.
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> . . . .
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> [T]he application of the securities laws to interests in employee benefit plans creates the potential for the imposition of large unforeseen liabilities, the termination of certain pension plans, the imposition of disclosure requirements which duplicate those of ERISA, and the addition of another body of law and another regulatory agency to an already crowded legal landscape.

85 Daily Labor Rep., Special Supp. (BNA) at 5-9 (May 2, 1978).

cally cannot be restricted to the facts of this case, to the broad class of participants in Teamster pension plans or even to employees who lost their pension interests prior to the effective date of ERISA. Employers, unions and Congress have conducted their affairs in the belief that the securities acts do not apply to involuntary, noncontributory pension plans. It is reasonable to assume that there are now in existence no retirement plans where the kind of disclosure which Daniel and the Seventh Circuit believe the securities acts require was made to employees at the time they voted to ratify a collective bargaining agreement, or were hired. This means that every retirement plan participant in the nation has at least a claim to benefits similar to Daniel's.

Moreover, even those employees who are protected by ERISA and who do not have a claim to benefits under its substantive provisions will have a claim against private pension plans and their sponsors. Thus, an employee terminated after five years of service—a term too short for the vesting of benefits to be required under ERISA—would have a claim under the Seventh Circuit's decision if all material facts concerning his potential pension benefits were not disclosed when he was hired or voted on the ratification of a collective bargaining agreement. Further, significant future liability may develop for failure to meet the basically unknown disclosure requirements of the securities acts as they apply to retirement plans. *See* pages 26-27, 28-31, *infra*.

Labeling such concerns a "parade of horribles" attributable to the zeal of advocates, the Seventh Circuit advised that "plan liability . . . is still limited

by a number of factors." 561 F.2d at 1250. This is not correct. The Seventh Circuit held the failure to disclose the actuarial probability that a participant will receive a pension to be a material omission.[13] Positive proof of reliance is not required for recovery in such cases. *Affiliated UTE Citizens* v. *United States*, 406 U.S. 128, 153-54 (1972). Moreover, statutes of limitations are not likely to reduce potential liability significantly in light of the fiduciary relationship between the sponsors, trustees and administrators of a plan and plan participants. That relationship may result in application of the federal "equitable tolling doctrine" until disclosure of the facts giving rise to a participant's potential cause of action or until the date he could begin receiving benefits—usually age 65. Indeed, the district court noted the applicability of that doctrine in this case. 410 F. Supp. at 544-45.

A conservative analysis of available data indicates that this present potential liability is staggering and, if it becomes reality by affirmance of the lower court's decision, could destroy the American private retirement plan system.

A study prepared by George B. Buck Consulting Actuaries, Inc. for the Department of Labor, indicates potential liability to be between \$23.8 billion and \$39.6 billion if all terminated non-vested partici-

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[13] Almost no plans have made such disclosures in the past. George B. Buck Consulting Actuaries, Inc., Report to the Secretary of Labor—*Potential Effect of Daniel*, unpublished study prepared under Contract J-9-P-7-0064 at II-2 (Mar. 20, 1978), available through Public Disclosure Room, Dept. of Labor, Pension and Welfare Benefit Programs, Room N4677, 3d Street & Constitution Ave., N.W., Washington, D.C. 20216.

pants are entitled to a pension and the applicable statutes of limitations runs from the participants' normal retirement date.[14] The study does not project the additional billions of dollars in liability that no doubt exist for presently employed workers who may someday receive no retirement benefits.[15]

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[14] *Id.* at III-1—III-3. The study estimates that this liability would be reduced to between $8.1 billion and $13.5 billion if the applicable statutes of limitations were to run from the date of termination of employment.

[15] If this Court sustains the Seventh Circuit, it should give serious consideration to applying its holding prospectively only. As this Court noted in *Los Angeles Dept. of Water & Power* v. *Manhart*, 46 U.S.L.W. 4347, 4352 (April 25, 1978), "the rules that apply to these funds should not be applied retroactively unless the legislature has plainly commanded that result." That conclusion certainly applies here, for Congress recognized that substantive regulation of retirement plans would impose new costs on the private pension system; costs which might jeopardize the continued existence of the very system it was striving to protect. Indeed, Congress made an express legislative decision not to make retroactive ERISA's break-in-service and vesting rules, 29 U.S.C. § 1053 (Supp. V 1975), which now preclude a person who, like Daniel, incurs a short break-in-service from losing his pension. The decision to limit ERISA to prospective application was the result of a clear compromise between the desire to remedy the problems of the private pension system through substantive regulation and the recognition of the need to do so without destroying its financial stability. *See Manhart, supra.* As Congressman Thompson stated on the floor of the House:

> I believe we have reconciled the competing interests of participants and pension plan sponsors in a way that speeds the protection of the new standards without creating undue financial dislocation or immediate disruption of existing pension plans. By way of explanation, I would draw the attention of my colleagues to the provisions dealing with the effective dates for the vesting, participation and eligibility provisions contained in part 2 of title I. Under the conference substitute the provisions with respect to participation and vesting will apply to new pension plans in plan years beginning after the date of enactment of the conference report. For pension plans in existence on January 1, 1974, the general effective date of the participation and vesting provisions is to be plan years beginning after December 31, 1975.

ERISA Leg. Hist., Vol. III at 4664. By granting Daniel the pension he seeks by retrospective application of the securities laws, this Court would destroy that compromise, in disregard of the command of the legislature.

If such a liability were imposed upon present retirement plans, many would be bankrupt, thus denying anticipated retirement benefits to all employees. Further, the lower court's decision raises the possibility of imposing that liability upon private companies which could jeopardize their very existence and the jobs and retirement expectations of millions of presently employed workers. Even more clearly, if such liability were imposed upon the nation's unions —as the Plaintiff herein seeks—they would be destroyed.[16]

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[16] The recent comments occasioned by a district court's review of an attempt to render unions liable for failure to police job site safety are relevant here:

> Union funds are derived from its members and only the largest unions may be potentially able to absorb the type of loss involved in this case. While unions may seek insurance coverage, the cost must be borne by the membership. Unions do not have finite limits of liability as do employers under workmen's compensation, nor can unions

If the decision of the Seventh Circuit is affirmed, the national policy of encouraging the expansion and creation of a retirement plan by making it possible for employers to provide benefits at a reasonable cost will be dealt a further blow by the cost of litigation which will result. With potential claims of billions of dollars, extensive litigation expense will confront defendant employers, unions and retirement plan administrators. If such suits are commenced as class actions, the potential liability realistically raises the specter of bankruptcy for employers, unions and retirement funds, thus increasing the motivation to settle even the seemingly most groundless claim. Nor is this mere speculation. The Plaintiff herein commenced his suit against the International Teamsters Union, all local Teamster unions, all trustees of all Teamster pension funds and all the officers of all Teamster unions, and did so on behalf of every Teamster member in the country who has participated in a Teamster pension fund.

Adding to these concerns is the lack of any statute or case law defining what must be disclosed regarding an involuntary, noncontributory retirement plan in order to meet the requirements of the securities

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> pass along such a loss to the public as may an employer. Moreover, the result is readily apparent, if unions could be held liable in cases such as this—there would be no negotiation on safety matters. To impose liability on the union in a case such as this is against public policy and would seriously disrupt labor relations policy.

House v. *Mine Safety Appliances Co.*, 417 F.Supp. 939, 946 (D.Idaho 1976).

acts.[17] For example, the Seventh Circuit held in this case that a plan must disclose "the actuarial probability, here perhaps as low as 8% . . . , that a member actually will receive pension benefits. . . ." 561 F.2d at 1229. It is not clear whether this refers to probability that a participant becomes eligible for a benefit or that he actually receives it. An employee who becomes eligible for a benefit, but dies in employment may not receive a benefit. Nor is it clear whether a uniform probability may be used for a plan as a whole or whether probability must be individualized and, if so, on what basis—type of job, geographic location, age or sex, etc. It is clear that in contrast to the carefully defined disclosure requirements of ERISA,[18] the development of disclosure requirements under the securities acts on a case-by-case basis will involve massive litigation.

Even in the absence of a national policy of encouraging the creation and expansion of retirement plans, the increased likelihood of antifraud litigation is a legitimate matter to be considered in construing the securities acts. In *Blue Chip Stamps* v. *Manor Drug*

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[17] What is "material" must be determined on a case-by-case basis. *See, e.g., SEC* v. *Shapiro,* 494 F.2d 1301, 1306 (2d Cir. 1974).

[18] *See, e.g.,* 29 U.S.C. §§ 1021-31 (Supp. V 1975); 29 C.F.R. § 2520.102-2, § 2520.102-3. It is clear that in enacting ERISA Congress did not intend that employers be confronted with an amorphous requirement to disclose all "material" information. Indeed, ERISA does not require disclosure of the "actuarial probability . . . that a member actually will receive pension benefits . . ." as would be required by the decision of the Seventh Circuit. 561 F.2d at 1229.

Stores, 421 U.S. 723 (1975), this Court recognized that:

> There has been widespread recognition that litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general.
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> . . .
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> [I]n the field of federal securities laws governing disclosure of information even a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial so long as he may prevent the suit from being resolved against him by dismissal or summary judgment.

421 U.S. at 739-40. Further, with respect to discovery, the Court stated:

> But to the extent that it [discovery] permits a plaintiff with a largely groundless claim to simply take up the time of a number of other people, with the right to do so representing an in terrorem increment of the settlement value, rather than a reasonably founded hope that the process will reveal relevant evidence, it is a social cost rather than a benefit. Yet to broadly expand the class of plaintiff who may sue under Rule 10b-5 would appear to encourage the least appealing aspect of the use of the discovery rules.

421 U.S. at 741.

In addition to spawning massive litigation, if affirmed, the decision of the Seventh Circuit negates the preemption of state law and elimination of in-

consistant and overlapping state regulation which is one of ERISA's key incentives to the expansion of the private pension system. The legislative history of ERISA indicates that Congress deliberately rejected a statutory approach that would have defined the areas of federal preemption of state law and, instead, enacted a broad preemption provision with only limited exceptions as an incentive to those sponsoring pension plans.[19]

On the House floor, Representative Dent characterized this approach in the following terms:

> Finally, I wish to make note of what is to many the crowning achievement of the legislation, the reservation to Federal authority of the sole power to regulate the field of employee benefit plans. With the preemption of the field, we round out the protection afforded participants

[19] As first presented to the House of Representatives, the proposed revision of the Welfare and Pension Plans Disclosure Act, H.R. 2, 93d Cong., 1st Sess. (1973), contained a preemption provision that delineated the areas in which the Act would supersede state law to those in which its provisions "may now or hereafter relate to the fiduciary, reporting, and disclosure responsibilities of persons acting on behalf of employee benefit plans." ERISA Leg. Hist., Vol. I at 50-51. Conference Committee action in June, 1974, however, resulted in a change of thrust by which ERISA § 514(a), 29 U.S.C. § 1144(a) (Supp. V 1975), now sets forth the general rule that the provisions of Titles I and IV of ERISA supersede *all* state laws relating to *any* employee benefit plan, and then lists specific exceptions, including the provision of § 514(b)(2)(A) that preemption does not apply "to exempt or relieve any person from any law of any State which regulates insurance, banking or securities." ERISA Leg. Hist., Vol. III at 4357.

by eliminating the threat of conflicting and inconsistent State and local regulation.

ERISA Leg. Hist., Vol. III at 4670. Senator Williams addressed the Senate [illegible] terms. ERISA Leg. Hist., Vol. III at 4745-46.

If, however, participation in an involuntary, noncontributory pension plan is an "investment contract" and therefore a "security," any state whose Blue Sky laws include an "investment contract" within the definition of a "security"[20] will be able to regulate pension plans in any manner not repugnant to the federal securities laws.[21] Since ERISA

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[20] To date, 33 states, Puerto Rico and the District of Columbia have adopted the Uniform Securities Act, whose definition of "security" in § 401(1) includes "investment contract." Most, if not all, of the other states also include "investment contract" in their definition of security.

[21] Section 18 of the Securities Act of 1933, 15 U.S.C. § 77r (1970), and Section 28(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb (1976), carefully and specifically save the jurisdiction of the states to regulate any security or person insofar as it does not conflict with or is not repugnant to the provisions of the federal securities laws. *See, e.g.*, *Crosby* v. *Weil*, 382 Ill. 538, 48 N.E.2d 386 (1943).

One state official, Willie R. Barnes, California Commissioner of Corporations, in the course of urging the Congress to permit greater state regulation in the area of employee welfare benefit plans, stated that *Daniel* had opened the way for a state to use its securities laws to regulate such plans. Oversight of ERISA, 1977: Hearings on S. 2125 Before the Subcomm. on Labor of the Comm. on Human Resources, 95th Cong., 1st Sess. 650, 681-83 (1977) (Statement of Willie R. Barnes).

preemption does not extend to state securities laws, 29 U.S.C. § 1144(b)(2)(A) (Supp. V 1975) (514 (b)(2)(A)), a state could establish extensive disclosure requirements inconsistent with those of ERISA and other states, thereby substantially increasing plan administrative costs. Given Congress' view that securities laws had only limited application to pension plans, this would permit the exception to swallow up the rule. The federal courts will then have undone the "crowning achievement" of the legislation passed by Congress in exposing sponsors of pension plans to "the threat of inconsistent State . . . regulations."

III. The Seventh Circuit's Decision Conflicts With The Realities Of The Employer-Employee Relationship And With Settled Labor Law Principles, Threatens Serious Disruption Of The Collective Bargaining Process And Is Contrary To National Labor Policy.

A. The Lower Court's Decision Ignores The Economic Realities Of The Employer-Employee Relationship And The Collective Bargaining Process.

The decision below casts the applicant for employment who takes a job and an employee who retains employment in the role of an investor under the securities laws. Nothing could be more foreign to the nature of the employment relationship. Employees are not investors and do not enter into investment relationships by accepting or continuing their employment. They supply labor, not capital, to the employing enterprise with one incidental aspect of the employment relationship possibly being participation in a retirement program paid for by their employer. Participation in such a retirement program is contingent upon the fact of employment alone.

The Seventh Circuit's securities law analysis employs a "literal approach" [22] and is squarely in conflict with *United Housing Foundation, Inc.* v. *Forman*, 421 U.S. 837 (1975). Writing for the majority in *Forman*, Mr. Justice Powell rejected the Second Circuit's use of this "literal" approach and clarified the thrust of the definition of "security" in the 1933 Act as follows:

> In providing this definition Congress did not attempt to articulate the relevant economic criteria for distinguishing "securities" from "non-securities." Rather, it sought to redefine "the term 'security' in sufficiently broad and general terms so as to include within that definition the many types of instruments that in our commercial world fall within the ordinary concept of the security."

421 U.S. at 847-48. Taking as a starting point the fact that the securities acts were passed to eliminate serious abuse in "the *capital* market of the enterprise system," the Court in *Forman* noted that an "investment contract" is in reality nothing other than an "instrument commonly known as a security," and concentrated on "economic reality" rather than superficial linguistic analysis. 421 U.S. at 849 (emphasis added). Using that framework, the Court ruled that the "stock" purchased by occupants of a cooperative apartment project was not a security subject to regulation under the federal securities laws stating:

> Well-settled principles enunciated by this Court establish that the shares purchased by respondents do not represent any of the "countless and

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[22] *See SEC* v. *W. J. Howey Co.,* 328 U.S. 293 (1946).

> variable schemes devised by those *who seek the use of the money of others* on the promise of profits" . . ., and therefore do not fall within "the ordinary concept of a security."

421 U.S. at 848 (emphasis added).

Unlike the shares purchased in the *Forman* case, Daniel's participation in a retirement plan was not labeled "stock." It is beyond argument, moreover, that participation in a noncontributory pension fund is not an "instrument commonly known as a security." As Judge Gesell, in *Robinson* v. *UMW Health and Retirement Fund*, 435 F.Supp. 245, 247 (D.D.C. 1977), observed:

> Yet until the 1975 [District Court] decision in *Daniel* (which predated *Forman*) no court had ever held, nor apparently had anyone including the SEC the temerity to argue that an interest in an involuntary, noncontributory pension or health benefit plan was covered by the securities laws.

Using the *Forman* economic reality analysis, it is clear that participation in a noncontributory retirement plan cannot be characterized as a security. Employees are not investors and are not entering into investment relationships by accepting or continuing their employment. They enter into an employment relationship, one aspect of which may be that if they contine to work for their employer for a certain number of years they will have a right to income at retirement. Indeed, this Court recently recognized that retirement plan coverage runs with the job and that employees normally do not make a decision to become or remain employed based upon the conditions of

their retirement plan. Thus, in *Los Angeles Dept. of Water & Power* v. *Manhart*, 46 U.S.L.W. 4347, 4351 n. 30 (April 25, 1978), this Court dismissed the contention that a gender-based distinction in retirement plan contributions was required in order to prevent male employees from withdrawing from the plan or their employment by stating: "[Y]et the Department points to no 'adverse selection' by the affected employees, presumably because an employee who wants to leave the plans must also leave his job, and few workers will quit because one of their fringe benefits could theoretically be obtained at a marginally lower price on the open market." To seize upon and mischaracterize one aspect of the total employment relation in order to label it (participation in a noncontributory pension plan) an "investment contract" and therefore a "security" is to do violence to the underlying economic reality.

Further, an analysis of retirement plans themselves indicates the folly of characterizing them as securities. As this Court recognized in *Alabama Power Co.* v. *Davis*, 431 U.S. 581, 593-94 (1977):

> [T]he "true nature" of the pension payment is a reward for length of service. The most significant factor pointing to this conclusion is the lengthy period required for pension rights to vest in the employee. It is difficult to maintain that a pension increment is deferred compensation for a year of actual service when it is only the passage of years in the same company's employ, and not the service rendered, that entitles the employee to that increment. Moreover, because of the vesting requirement and the use of payment formulas that depend on earnings at the time of retirement, both the cost to the employer and the payment to the employee for each year of service depend directly on the length of time the employee continues to work for that employer.[23]

Thus, an employee under a noncontributory retirement plan does not choose to take part of his wages and invest them with the employer in the hope of making a profit; retirement income is conditional deferred compensation in the sense that it is given only after a fixed number of years of service. An investor in securities, on the other hand, is not provided with additional compensation for services rendered. Quite the contrary, the investor supplies capital, not labor, to a business enterprise. By characterizing participation in a retirement plan as a security, the Seventh Circuit's decision obliterates the fundamental distinction between capital and labor upon which the American economic system is based.

Moreover, retirement plan participation in the context of ratifying a collective bargaining agreement cannot in any realistic sense be characterized as a

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[23] Even ERISA has not changed this system; it simply has imposed reasonable requirements on the length of time it takes for the employee to attain a "vested" right. As was observed in House Report No. 533: "[ERISA] presumes that promised pension benefits are in the form of a conditional deferred wage. While popular attention focuses on the deferred wage aspect of pensions, the Act recognizes that the pension promise is conditional upon completion of minimum periods of service." ERISA Leg. Hist., Vol. II at 2360.

"sale" under the securities acts. The lower court's opinion assumes that employees pay for or "buy" retirement benefits because they voluntarily (by their vote to ratify a union-negotiated agreement) give up present wage increases in exchange for the employer's contribution to pensions. But that conclusion is at odds with the nature of collective bargaining for a number of reasons.

First, even union-represented employees do not have a choice as to what wages and retirement benefits their employer will pay. The American retirement system is a voluntary system in which employers are free to provide or not to provide retirement benefits. Nothing in the national labor policy supporting collective bargaining requires that any employer provide retirement benefits; all the National Labor Relations Act requires is that employers bargain about retirement programs, not that they be provided. *Inland Steel Co.* v. *NLRB*, 170 F.2d 247 (7th Cir. 1948), *cert. denied*, 336 U.S. 960 (1949); *H. K. Porter Co.* v. *NLRB*, 397 U.S. 99 (1970).[34]

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[34] The term "bargaining in good faith" . . . is a word of art. . . . As applied to a particular term and condition of employment such as pensions, it would mean simply . . . that an employer must discuss it with an open mind—if it is brought up. It would not mean that an employer has to offer a pension program in general or a particular pension proposal, or even accept the concept of pensions at all. It surely does not require that an employer agree to any pension proposal at all.

ERISA Leg. Hist., Vol. III at 3540.

Thus, an employee vote to drop a retirement program may be rejected by an employer who insists upon providing retirement benefits to retain long-term employees. Or that vote may be accepted but yield little or no additional cash wages, for a dollar paid into a retirement program has a different value to an employer than a dollar paid in cash wages because of different tax consequences, social security levies and overtime pay requirements.

Second, bargaining agreements cover many components of an employment relationship other than retirement benefits and wages.[35] Collective bargaining negotiations typically are conducted in sophisticated relationships by means of "package" proposals. These packages deal with many items under discussion.

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[35] The provisions of a collective bargaining agreement may cover, in addition to retirement arrangements, such subjects as union security; check-off of union dues; seniority rights; job protection; provisions for layoff and recall from work; wages, special overtime, call-in, shift and reporting pay; the employer's right to subcontract work; the employer's right to discipline or discharge employees; a definition of management's rights; vacations; holidays; cost of living pay adjustment provisions; grievance and arbitration procedures; nondiscrimination pledges; union hiring hall procedures; hospitalization insurance protection; life insurance protection; severance pay; no-strike and no-lockout commitments; matters covering employee safety; leaves of absence; procedures for job assignments and job bidding; incentive and bonus plans; break periods; parking privileges; eating facilities; apprenticeship and training programs. *See Manual for Drafting Union Contracts* (Prentice Hall 1969).

When a final proposal is hammered out and submitted for ratification, it is presented as an entire package. To assume, as the Seventh Circuit did, that employees then separate wages and retirement benefits from that package and consider them in a vacuum is unrealistic because it assumes that employees have little interest in such employment conditions as seniority protection, holidays, vacations, extra overtime compensation, cost of living wage escalators, and insurance benefits.

Finally, the lower court's decision also is premised on the assumption that unions and employees in the ratification process make decisions based upon a rational evaluation of the substantive work-related proposals before them. Nothing in the law[26] or human nature lends required support for that assumption. Thus, for example, employees may vote to accept an agreement simply because they cannot afford to strike,[27] or vote to reject the agreement and strike because they are irritated about something unrelated to the bargaining agreement.[28]

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[26] "The system has not reached the ideal of the philosophic notion that perfect understanding among people would lead to perfect agreement among them on values." *NLRB* v. *Insurance Agents International*, 361 U.S. 477, 488-89 (1960).

[27] *See NLRB* v. *Granite State Joint Board*, 409 U.S. 213, 217 (1972).

[28] *See Ready Mixed Concrete, Inc.*, 200 NLRB 253 (1972), in which a union picketed to put the employer out of business because of what it believed to be a breach of faith by the employer which resulted in a heart attack suffered by the union's secretary-treasurer.

In sum, nothing about the employment relationship or the collective bargaining process supports the conclusion of the court below that employees are securities buyers and investors when they acquire or retain employment or when they vote to ratify a union-negotiated agreement providing for involuntary, noncontributory retirement plan participation.

B. The Decision Of The Court Below Conflicts With Labor Law's Exclusivity Principle And Threatens To Disrupt The Collective Bargaining Processes.

The lower court's decision is in direct conflict with national labor policy. The Seventh Circuit determined that at least one occasion on which a "sale" of a "security" (a retirement plan) is made to union-represented employees is when those employees vote "whether or not to accept the collective bargaining contract containing . . . [a] pension fund and whether to ratify subsequent agreements governing the level of employer contributions into the fund. . . ." 561 F.2d at 1243. Accordingly, the lower court ruled that because the ratification process results in employees choosing to accept or reject retirement plan coverage instead of higher wages, they must be provided with material facts relating to the retirement plan before they vote.

This determination derogates from the cornerstone of the national labor policy—the principle of union bargaining agent exclusivity.

Under that principle, once a union is chosen by employees to represent them, it is that union, and only that union, which may bargain with an employer over employment terms. Employees no longer may bargain individually or in groups with their em-

ployer, and for good reasons. By combining into one group and designating the union as their sole negotiator, employees pool their economic strength and may more effectively seek improvements in their working conditions. Further, as long as the union remains the sole employee voice with their employer, that employer may not splinter the cohesive unit of employees by granting different benefits to different interest groups. From the employer's perspective, it need deal with only a single set of wage and benefit demands thus facilitating ultimate agreement and reducing the threat of strikes which adversely effect its business and the nation's economy. In sum, both in theory and in practice, the exclusivity of the union bargaining representative has been the key to an effective national labor policy.

This Court not only has endorsed the principle, but also emphatically has rejected attacks on it from many quarters. *See, e.g., Emporium Capwell Co.* v. *Western Addition Community Organization*, 420 U.S. 50 (1975). For example, this Court has held that when employees have duly authorized a union to represent them for collective bargaining, the union becomes their sole and exclusive agent in dealing with the employer for and on behalf of employees represented by it. *NLRB* v. *Allis-Chalmers Mfg. Co.*, 388 U.S. 175 (1967); *J.I. Case Co.* v. *NLRB*, 321 U.S. 332 (1944); *Medo Photo Supply Corp.* v. *NLRB*, 321 U.S. 678 (1944). As this Court has remarked, "only the union may contract the employee's terms and conditions of employment. . . . The employee may disagree with many of the union decisions but is bound by them." *NLRB* v. *Allis-Chalmers Mfg. Co.*, 388 U.S. 175, 180 (1967).

Accordingly, an employer violates its good faith bargaining obligation imposed by Section 8(a)(5) of the National Labor Relations Act, 29 U.S.C. 158 (a)(5) (1970), when it bypasses the exclusive bargaining agent without its consent and bargains directly or individually with the employees it represents concerning wages, hours and other conditions of employment. *NLRB* v. *Insurance Agents' Internat'l*, 361 U.S. 477, 484-85 (1960); *Medo Photo Supply Corp.* v. *NLRB*, 321 U.S. 678 (1944); *United Steelworkers of America* v. *NLRB*, 536 F.2d 550 (3d Cir. 1976), *on remand*, 227 NLRB 1005 (1977); *NLRB* v. *General Electric Co.*, 418 F.2d 736 (2d Cir. 1969), *cert. denied*, 397 U.S. 965 (1970). Indeed, employees who attempt to bargain directly with their employer in derogation of their exclusive bargaining representative may be discharged lawfully. *Emporium Capwell Co.* v. *Western Addition Community Organization*, 420 U.S. 50 (1975).

Consistent with this formulation of labor policy, this Court also has ruled that employer insistence on a contractual right to require that certain procedures be followed by employees before their exclusive representative may call a strike or refuse an employer's offer of a new bargaining agreement also contravenes the employer's good faith bargaining obligation by improperly injecting the employer into internal relations between employees and their bargaining representative. *NLRB* v. *Wooster Division of Borg-Warner Corp.*, 356 U.S. 342 (1958). In those cases, moreover, where the union has established a contract ratification process in which employees vote to determine whether or not the union will reach an agreement with the employer, the employer may not

insist that its bargaining proposals be submitted to an employee vote. *Houchens Market of Elizabethtown, Inc.* v. *NLRB*, 375 F.2d 208 (6th Cir. 1967). If proposals are presented to employees for ratification, the employer may not even be present at the ratification meeting, because it is settled labor law that employers are precluded from intruding upon procedures by which employees decide to accept or reject a proposed contract. *See, e.g., Mon River Towing, Inc.* v. *NLRB*, 421 F.2d 1, 8 (3d Cir. 1969); *Amalgamated Meat Cutters & Butcher W.* v. *NLRB*, 276 F.2d 34 (1st Cir. 1960); *Nassau & Suffolk Contractors' Ass'n*, 118 NLRB 174 (1957). Finally, no union is required to establish a contract ratification procedure for the employees it represents, and employees have no right to insist that their union do so.[29] *Houchens Market of Elizabethtown, Inc.* v. *NLRB*, 375 F.2d 208 (6th Cir. 1967); *Cleveland Orchestra Comm.* v. *Cleveland Fed. of Musicians*, 303 F.2d 229 (6th Cir. 1962).

[29] Even if a union has established a ratification procedure, its purpose under labor law principles is not to bring employees into the bargaining process but rather, it exists as a mechanism by which the union decides whether or not to enter into an agreement with an employer. *Houchens Market of Elizabethtown, Inc.* v. *NLRB*, 375 F.2d 208 (6th Cir. 1967). Thus, a union spokesman with express or apparent authority to enter into an agreement with an employer must sign a bargained-for agreement binding all represented employees, even though he or she claims that the agreement must first be submitted to employees for ratification; even when the union's constitution requires such prior ratification; and even where the employees, in fact, have voted and rejected the agreement. *National Elevator Industry, Inc.*, 185 NLRB 769 (1970), *enforced*, 465 F.2d 974 (9th Cir. 1972); *Associated Bldg. Contractors of Evansville, Inc.*, 143 NLRB 678 (1963), *enforced in relevant part*, 334 F.2d 729 (7th Cir. 1964).

By these and similar decisions, the courts and Labor Board have maintained unions as exclusive employee representatives and have established collective bargaining as an effective instrument of our national labor policy.[30]

Wholly apart from the fact, discussed above, that voting to ratify a collective bargaining agreement including retirement plan benefits, does not constitute an investment transaction or the purchase of a security, the lower court's decision will require serious disruption of collective bargaining relationships by forcing employers to intrude upon internal union procedures and to bargain directly with employees in derogation of the exclusive bargaining representative.

As a direct consequence of the lower court's decision, no prudent employer, faced with the prospect of damage claims resulting from a union's failure to disclose fully all material aspects of a retirement plan to employees,[31] can rely safely upon the union to

[30] This is not to suggest that individual employees have no rights. Indeed, they may sue their employer for breach of their contractual rights and may sue their union if it has breached its duty to represent all employees fairly, impartially and non-discriminatorily. *See, e.g., Vaca* v. *Sipes*, 386 U.S. 171 (1967); *Hines* v. *Anchor Motor Freight, Inc.*, 424 U.S. 554 (1976); *Bryant* v. *International Union*, 467 F.2d 1 (6th Cir. 1972), *cert. denied*, 410 U.S. 930 (1973); *House* v. *Mine Safety Appliances Co.*, 417 F.Supp. 939 (D. Idaho 1976).

[31] Although the Seventh Circuit made no such finding, employer liability for failure of a union to disclose all material facts may be based upon the theory that he aided and abetted

make the required disclosures. Thus, the employer must at least attend any union ratification meeting to insure that proper disclosures are made and that nothing is misrepresented to employees. If the lower court's decision is correct, the employer will be required to discuss with the assembled employees the trade-offs associated with the decision to offer specified levels of cash wages and retirement benefits, *e.g.*, whether more wages would be paid if no retirement benefits were provided and, if so, how much more. In sum, the employer will have to reopen the bargaining process and deal with individual employees in an effort to provide them with the information they need to make an informed decision.

The justifications advanced by the court below to minimize the impact of this result on the bargaining process cannot withstand analysis and demonstrate a logical inconsistency fatal to the court's reasoning.

First, the circuit court suggested that because the sale to employees which triggers the need for disclosure ". . . would *normally* occur when an employee decides to accept or continue a job . . . ." 561 F.2d at 1249 (emphasis added), there will be no adverse effect on bargaining because those employee decisions are unrelated to bargaining. The difficulty with the

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in the sale of the security (the retirement plan), or may be based upon analogous theories. Accordingly, any employer must conduct his bargaining in a manner calculated to protect itself from potential damages under the securities acts. *See, e.g., Hines* v. *Anchor Motor Freight, Inc.*, 424 U.S. 554 (1976); *Johnson* v. *Goodyear Tire & Rubber Co.*, 491 F.2d 1364 (5th Cir. 1974); *In re Caesars Palace Securities Litigation*, 360 F.Supp. 366 (S.D.N.Y. 1973).

court's cavalier conclusion is that just because decisions to accept or continue employment trigger the requirement of disclosure does not mean that a ratification vote also does not trigger that same requirement. Indeed, the court recognized that fact by its use of the word "normally." Further, if a decision to accept or continue in a job, which does not involve an employee vote on specific employment terms, triggers a requirement of disclosure, than *a fortiori* the employee ratification vote also must trigger disclosure. Finally, the Seventh Circuit found that a sale is triggered at the time employees vote on a union negotiated agreement. 561 F.2d at 1243.

Second, the court discussed employee ratification votes in order to establish that employees voluntarily buy pensions. 561 F.2d at 1243. However, because the court also found that a sale may occur under the securities acts even without volition, the court's finding of volition in the ratification vote may be said to be superfluous and, accordingly, disclosures need not be made prior to such a vote. Such an argument overlooks the fact that disclosure has to be "triggered" by some event whether or not that trigger involves volition, otherwise no one will ever know when to make the required disclosures. Accordingly, if, as discussed above, an employee's acceptance or retention of a job is such a trigger, surely a contract ratification vote also must trigger a sale.

In sum, even if employee decisions to accept or continue employment trigger the antifraud provisions and even if volition is not required, the antifraud provisions and their required disclosures still are triggered by an employee ratification vote with the consequences discussed above.

C. The Seventh Circuit's Decision Also Conflicts With Other Goals Of National Labor Policy.

The lower court's decision also may lead to disruption of the labor policy's basic goal of lessening labor strife. *See* 29 U.S.C. § 141 (1970); *United Steelworkers of America, AFL-CIO* v. *NLRB*, 530 F.2d 266, 275 (3d Cir.), *cert. denied sub nom. Dow Chemical Co.* v. *United Steelworkers of America*, 429 U.S. 834 (1976). The time that will be required to comply with security law disclosure rules will complicate orderly bargaining and contribute to strife. For example, if in support of its demands leading to an eventual agreement, a union's membership strikes an employer in part because of a dispute about retirement benefits, it is likely that the work stoppage may be prolonged following a bargaining table agreement reached between the employer and the union because of the complexity of modern retirement plans and the actuarial, financial and legal analyses necessary to comply with disclosure requirements prior to a ratification vote. Nothing could be more disruptive of stable labor-management relations and the free flow of commerce.[32]

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[32] The recent decision of this Court in *Federal Maritime Comm.* v. *Pacific Maritime Ass'n*, 46 U.S.L.W. 4169 (Mar. 1, 1978), in no way detracts from the discussion above. That case involved the claim by the Pacific Maritime Association ("PMA") that agreements bargained with the International Longshoremen's and Warehousemen's Union did not have to be filed for approval with the Federal Maritime Commission under Section 15 of the Shipping Act, 1916, 46 U.S.C. § 814 (1970). The major contention of the PMA was that such a requirement would disrupt collective bargaining and labor peace for no union-management agreement could be implemented until the Commission approved it. This Court rejected

The Seventh Circuit's decision also may discourage unions from bargaining about retirement benefits. Any union that bargains for retirement plan benefits exposes itself to potential damage claims if it does not disclose all material facts to employees. Because no one knows what facts the courts ulti-

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that contention, but on grounds which reinforce, rather than detract from, the adverse effects of securities acts' coverage of collectively bargained retirement plans.

Thus, this Court noted that not all collectively bargained agreements would have to be filed with the Commission (*e.g.*, single employer-union agreements). Further, agreements dealing only with mandatory collective bargaining subjects (wages, hours and working conditions of employees within the bargained-for unit) would be routinely approved. Others could be quickly approved conditionally by the Commission. Accordingly, this Court concluded that no extensive delay harmful to the institution of collective bargaining would result from a requirement that some agreement be filed and approved by the Commission.

On the other hand, applying the securities acts to negotiated retirement plans has an impact on every contract containing retirement plan coverage even though the latter is a mandatory bargaining subject. Thus, in every instance employers will seek to attend union ratification meetings and fully explain the retirement plans. In addition, every such ratification meeting will be delayed while lawyers, actuaries and accountants try to determine every fact, calculation and assumption which must be revealed—for there is no such thing as quick, predisclosure, conditional approval by a governmental agency which protects employers and unions from liability under the antifraud provisions of the securities acts. As this Court recently observed: "The court should have taken into account the difficulty of amending a major pension plan, a task that cannot be accomplished overnight." *Los Angeles Dept. of Water & Power* v. *Manhart*, 46 U.S.L.W. 4347, 4352 n. 36 (April 25, 1978).

mately may decide are "material," [33] the only way unions may completely protect themselves is to decline to bargain with employers concerning retirement benefits.[34] To encourage such action by unions would deprive employees of the collective strength of their representative in pension bargaining. As the Sixth Circuit correctly concluded in an analogous situation: "[S]uch . . . would simply deter unions from engaging in the unfettered give and take negotiation which lies at the heart of the collective bargaining agreement . . . . Such result would not serve the interest of . . . [employees] and would retard rather than advance the goals of the National Labor policy." *Bryant* v. *International Union*, 467 F.2d 1, 5, 6 (6th Cir. 1972), *cert. denied*, 410 U.S. 930 (1973). *See also House* v. *Mine Safety Appliances Co.*, 417 F. Supp. 939 (D. Idaho 1976).

[33] *See* note 17, *supra*.

[34] The removal of retirement benefit agreements from a contract ratification process might not insulate unions from liability under the lower court's theories, which also require disclosures of retirement plan material facts when an employee accepts or retains a job. Thus, the only way a union can completely avoid liability under the securities acts is to avoid bargaining about pension benefits. This emphasizes the fallacy of the lower court's argument that its decision will have no adverse impact on the collective bargaining process.

IV. Conclusion.

The decision of the Seventh Circuit in *Daniel* is directly at odds with congressional policy for it disrupts the delicately balanced provisions of ERISA which protect the plan participant without discouraging the growth and development of the private pension system. The decision further threatens serious disruption of national labor policy.

Accordingly, it is respectfully submitted that the judgment of the Court of Appeals for the Seventh Circuit is in error and should be reversed.

Respectfully submitted,

Peter G. Nash
George J. Pantos
1750 Pennsylvania Ave., N.W.
Washington, D.C. 20006

Thomas L. O'Brien
Arthur B. Smith, Jr.
115 South LaSalle Street
Chicago, Illinois 60603

Counsel for ERISA Industry Committee, amicus curiae